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EAST-WEST TRADE  
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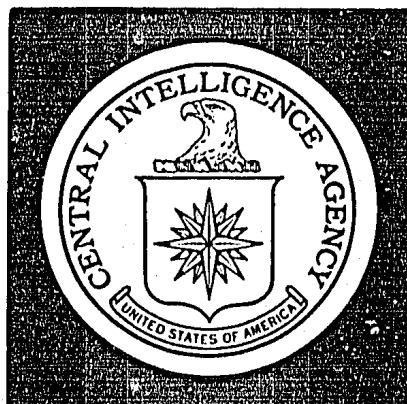
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DIRECTORATE OF  
INTELLIGENCE

# Intelligence Memorandum

*The Growing Barter Element In East-West Trade*

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CENTRAL INTELLIGENCE AGENCY

Directorate of Intelligence

June 1970

INTELLIGENCE MEMORANDUM

The Growing Barter Element In East-West Trade

Introduction

Trade between Eastern and Western Europe from the end of World War II until 1958 was conducted chiefly through bilateral clearing. In 1958, most West European currencies were made freely convertible, and the general trend since that time has been toward settlements in convertible currency. In the recent past, however, barter deals in East-West trade have increased noticeably. This memorandum discusses the various types of barter arrangements between the two country groupings and assesses the role of barter trade in East-West commercial exchanges.

Background

1. The introduction of convertibility of major Western currencies in 1958 brought with it a decline in the importance of bilateral clearing as a means of settling trade accounts between East and West.\* The clearing form of agreement has given way largely to arrangements to settle trade accounts in convertible currencies. About one-fourth of today's East-West trade is still handled formally on a clearing basis. While this accounts for a significant portion of total East-West trade, it results largely from special arrangements, which include the German interzonal trade (West Germany's only clearing arrangement) as well as the special trade relations of Finland with the USSR.\*\* During 1964-67, ten clearing agreements were terminated involving the USSR, Poland, Romania, Czechoslovakia, Norway, Sweden, France, Denmark, and Iceland. The USSR and Austria are now negotiating the termination of their clearing agreement.

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*Note: This memorandum was produced solely by CIA. It was prepared by the Office of Economic Research.*

*\* Unless otherwise specified, West refers to the Industrial West and East-West trade means the trade of the USSR and Eastern Europe with the Industrial West.*

*\*\* In 1968, about \$2.8 billion of the approximately \$10 billion volume of East-West trade was conducted on a clearing basis. About \$1.1 billion of this included the German interzonal trade and Soviet trade with Finland. Four Western countries (Austria, Finland, West Germany, and Switzerland) and two Eastern countries (the USSR and East Germany) are the main clearing partners.*

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**CONFIDENTIAL****Types of Barter**

2. The existence of agreements to settle accounts in convertible currency notwithstanding, the USSR and East European countries are engaging more extensively in barter transactions with firms in Western countries than in the past. Western companies engaged in barter deals with the USSR and East European countries usually break down these transactions into three types.\* The classic barter arrangement of a straight exchange of goods in East-West trade apparently is on the decline, although sizable transactions are still reported. Some examples in 1970 include the exchange of 400 Japanese passenger cars for Czechoslovak tractors, and the exchange of 5,000 British passenger cars for various Hungarian manufactured articles.

3. Switch trading—a second category—has been in vogue for a number of years in transactions between East and West. The necessary ingredient in switch trading is a clearing agreement. When the clearing accounts are in a state of imbalance and the goods offered by the deficit country are not wanted by the creditor country, the switch trader may offer to buy from the central bank or other appropriate financial institution of the creditor country, at a discount, some of the “clearing units” in which the accounts are maintained. He then sells these clearing units to a third country which is willing to buy the goods offered by the deficit country. The bilateral imbalance is thus reduced. In 1967, for example, switch trading offset as much as \$40 million in Austrian surpluses with Communist countries.\*\* As long as clearing agreements are in operation, switch trading will persist; the declining number of clearing agreements suggests that this form of barter is on the way out. Moreover, the International Monetary Fund (IMF) is pressuring its members to terminate such arrangements because the concessions needed to make switch deals attractive, such as discounts, in effect have introduced multiple exchange rates in member countries’ trade, a violation of IMF rules.

4. A third category of barter, known as “compensation” trading, generally calls for the Western supplier to be paid partly in cash with the balance in counter deliveries of goods. This type of barter arrangement has been used with increasing frequency in contrast with the declining use of the two previously mentioned forms. According to recent reports, it is not

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\* For a selective listing of major barter deals, see the Appendix.

\*\* Switch traders operate mainly in Vienna and Zurich. In 1967, switch volume was estimated at about \$150 million in Zurich and roughly \$120 million in Vienna. Not all transactions, however, involved East-West trade.

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uncommon for a Western partner to accept 10% or 15% of the value of its sale in counter purchases. British sales contracts with Polish customers often require that the British take 20% of the contract value in Polish goods, but British dissatisfaction with the quality of Polish commodities usually has resulted in this clause being honored more in the breach than in the fulfillment.

5. A variation on the compensation-type transaction, and one that is becoming increasingly popular for high-value transactions, involves a combination of credit and barter. Thus, the Western supplier extends a medium- or long-term credit to the Eastern partner and is to be repaid partly or wholly in goods, often goods produced from the plant and equipment provided on credit. Some examples of this type of agreement in the past two years include the 1968 Soviet agreement with Japan whereby Japan is to furnish \$130 million in equipment on a 5-year credit to develop Siberian forest resources. Repayment is being made from the proceeds of the sale of lumber produced by the Japanese equipment.\* In another example, a contract involving Hungary, France, and West Germany calls for repayment in both goods and foreign exchange. The Western countries are to deliver and install a diesel engine plant valued at \$22 million. The 8-year credit extended is to be repaid in hard currency (70%) and Hungarian goods (30%) including \$1.5 million worth of engines from the diesel engine plant. Other important contracts of this type include the arrangement between a British consortium and Romania whereby the British group will deliver \$53 million in irrigation facilities and equipment, with \$43 million on an 11-year credit. Repayment is to be in the form of agricultural goods produced in the irrigated area. The largest of the credit-compensation contracts are those involving the delivery of West German and Italian pipe and equipment to the USSR to build natural gas pipelines, with repayment over a long period of time in natural gas. The value of the pipe for natural gas contracts is in the hundreds of millions of dollars.

**Barter Trade Facilities**

6. Facilities have been and continue to be developed in the West to deal with the problem of handling numerous barter arrangements in East-West trade. In Europe, merchant banks now have compensation departments. Even in the United Kingdom, which had lagged behind its competitors on the Continent in the pursuit of barter, about 30 companies, British and foreign, were working on compensation deals in 1968. Of these, ten are

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\* A similar Soviet-Japanese credit-compensation agreement involving \$350 million in Japanese plant and equipment on 10 years' credit is pending.

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considered specialists and as many as five do nothing else. In 1968, an agency was formed in Hamburg for the specific purpose of fostering barter and switch deals between West German exporters and CEMA country enterprises. This company is called the Internationale Compensationcentrale Gesellschaft fuer Export-Import-Koordinierung (ICC) and is jointly owned by the Institut fuer Ost-Marktforschung GmbH and Glahe International of Cologne. More recently, an East-West trade syndicate was set up in Paris to help French enterprises satisfy the conditions of bilateral purchasing agreements with the USSR and Eastern Europe by providing easier outlets in France for goods imported from these countries. Behind the syndicate are four French banks, including Credit Lyonnais, Societe Generale, Credit Commercial de France, and the Soviet-owned Banque Commerciale pour l'Europe du Nord (BCEN).

**Continuing Demand for Barter**

7. A dozen years after the return to convertibility by West European countries, barter is still an important element in East-West trade. As East-West trade has grown, barter has persisted--in large part because of the continued inability of the USSR and East European countries to produce marketable goods in sufficient quantities to generate required hard currency earnings. Hard pressed to earn the required amounts of foreign exchange, and lacking adequate financial reserves, these countries strive to balance trade with each Western trading partner. This approach to trade, moreover, is consistent with the planning of foreign trade and is especially appealing to the central planner in that it reduces the uncertainty associated with trading in "capitalist" markets. Barter, moreover, makes use of the Western trading partners' access to and experience with marketing channels in the West. Communist traders, as a consequence, have a barter mentality.

8. Since 1958, there has also been a steady increase in the use of Western credit facilities to help breach the gap between the East's desire to import and its ability to pay for Western goods. At present, Soviet and East European outstanding medium- and long-term indebtedness to the West is on the order of \$4 billion. The extension of such credits has been instrumental in raising the level of East-West trade to new heights but in itself has not enhanced the ability of the Eastern countries to expand sales to the West. Now these credits are being combined with barter in a number of deals, and in this way the Communist countries are helping to guarantee for themselves the wherewithal to repay the Western credits through expansion of exports. In fact, within a year or so, about \$1 billion in Eastern indebtedness to the West will be comprised of credits with repayment provisions involving barter.

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9. As it takes two to make a deal, however, the successful conclusion of various barter agreements, particularly those involving credit, indicates increased Western acceptance of East European demands for concessions in return for the placement of orders in the West. Indeed, the growing institutionalization of barter via organizations and banking departments specializing in East-West barter suggests that many Western businessmen anticipate that barter between East and West will be around for a long time.

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SWEDEN; TELEPHONE: 0303/91835; TELEX: 2422**

HEFA AB, 1010 Vienna, Parkring 10;  
Tel: 52 22 14; Telex: 13392.

HEFA AB, Bucharest/Romania, Cimpia Turzii 21;  
Tel: 17 73 43; Telex: 297

Financial Times, 11 Feb 70

### Conclusions

10. Following the return to convertibility of West European currencies in 1958, there was a decline in the use of bilateral clearing accounts and of barter in East-West trade. In recent years, however, barter transactions have become a more important element in East-West trade.

11. Among other things, use of barter, especially the increasing role of compensation trading in East-West trade, is a function of the continuing inability of the USSR and East European countries to produce marketable goods in sufficient quantities to foster the growth of their trade with the West. In turn, Western exporters, anxious to expand their sales, have agreed to take—at least in partial payment-counterdeliveries of goods often produced by the Western equipment originally purchased, and have made long-term credit a part of many deals.



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12. In the meantime, facilities continue to be developed in the West to meet the growing requirements of barter trade. In addition to the growth of "compensation" departments in European merchant banks, special companies are being formed for the sole purpose of promoting East-West barter trade. This suggests that Western firms regard barter as a more or less permanent feature of East-West trade and that they see little prospect of the East European countries independently improving their capabilities to upgrade exports to the West in the near future.

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